

**TESTIMONY BEFORE THE HOUSE COMMITTEE ON BANKING AND FINANCIAL SERVICES
REGARDING PREDATORY MORTGAGE LENDING**

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Good morning. I am an attorney with Legal Aid of Western Michigan. I've been an attorney with Legal Aid for over seven years; for the last year and a half I have had the privilege of holding a fellowship awarded by the National Consumer Law Center and National Legal Aid and Defender Association that has allowed me to focus my practice nearly exclusively on consumer law and predatory mortgage lending cases.

It was hard to decide where to begin and what stories to share with you. For so many of the homeowners I meet the American dream has become the American nightmare. Some families are trying to own their first home and piece together a better life for their children and it is falling down around them. Others have lived in their house for years, perhaps raised their children and grandchildren in the home, and now they are losing that home.

Consider one family living in Grand Rapids. A husband and wife who have raised their own children and have now opened their home to foster children. They received a cold call from a mortgage company promising a fixed rate mortgage with an interest rate of 6.8%. They would get some cash back and be able to pay off some bills. They were provided with documents that showed those terms. The homeowners were pleased, believing that they were getting a good deal. They were especially pleased that they would be getting a fixed rate, as they felt that was important given their income was primarily from Social Security. A notary came to their house and rushed them through signing an inch thick stack of documents. They were not given these loan documents before hand. They were not given a chance to ask questions.

They eventually had some questions and came to my office. Contrary to what the mortgage broker had promised, they ended up with an adjustable rate mortgage with a 24 month teaser rate of 6.650%. The initial payments were \$791.23 per month. After the two year teaser rate adjusts, based upon the interest rates at the time this loan closed in November 2005, the payments were scheduled to increase more than \$200 per month. Over the life of this loan, the interest rate can go as high as 12.65%. When I told this to the homeowners, the look on their faces told me that they had no idea what they had signed. There is no way they could afford a payment of nearly \$1000 per month.

The homeowners were also required to pay \$10,492.54 in settlement charges and closing costs to receive a total benefit of \$8460.54 in cash and payoffs. A substantial portion of the fees went in the mortgage broker's pocket for his work on this loan. In fact, the mortgage brokers were asking for such

a high commission that the lender initially refused to approve it, but when the mortgage broker lowered the amount designated as their fee and categorized the difference as a "processing fee" the lender then approved the total fees to the broker. This is on top of the yield spread premium paid by the lender to the mortgage broker.

We obtained Judgments against the mortgage broker and the title office but have no real hope of collecting on them because they are located out of state and appear to have gone out of business. The lender filed for bankruptcy during our case so we are waiting for that to resolve and are hoping that maybe, someday, they will receive some small compensation. Meanwhile the homeowners refinanced with another mortgage company before the interest rate adjusted, although they had to pay a prepayment penalty to do so.

Federal Judge Richard Enslen described another one of my cases this way, "The crooks in prison wear...are easy to spot. Those in business wear are not; though they do no less harm to their unsuspecting victims."

The homeowner in this case lives in Ionia County. She purchased the house in 1977. She wanted to refinance her home to get a little bit of cash for some repairs and to pay off a credit card. Money was tight because her only income was her Social Security Disability check. She received a flyer for a mortgage broker and so she contacted them. One of their employees came to her home and had her sign an application. She told that employee what she was looking for, and he told her he would be able to get her a mortgage with a lower, fixed interest rate, would pay the credit card, and give her that cash back. She signed an application for a fixed rate loan and was given estimates for a fixed rate loan.

However, when a notary came to her house to sign the final documents, this homeowner was concerned. The notary was late, several days late in fact, and the homeowner did not have time to review the documents prior to the notary's arrival. At the closing, the homeowner discovered that the mortgage broker had falsified employment information. She received Social Security Disability and had not worked in years; however, a new application in the closing packet listed an employer and a substantial income. The homeowner pointed this out to the notary, but was told that it would be corrected. Because the notary was in her home, and because the notary had been late, and because she thought she could trust the mortgage broker, the homeowner signed for the loan.

What this homeowner ended up with was far different than what she wanted. Her initial teaser interest rate was 7.99%. After the first twenty four months her interest rate would increase dramatically to the LIBOR index plus 7.49%. This means that, based upon the interest rates at the time the loan closed, her interest rate would adjust to about 11.9367%. Her payments would go from \$454.50 per month under the teaser rate to \$602.66 per month, again, assuming that interest rates remain the same as they were at close. And the credit card she wanted paid off? Did not get paid off.

In addition, this homeowner also paid a substantial amount of points and fees, in excess of 6%. A substantial portion of these points and fees went into the broker's pocket with the approval of the lender. In this loan the lender paid the mortgage broker a yield spread premium. Identified on the closing documents as "YSP POC," many homeowners are unaware of what this fee is or what it means for them. Basically, it is a cash payment the lender gives to the mortgage broker for "upselling" the loan, that is, getting the homeowner to accept a higher interest rate than what they actually qualify for. In this case, the yield spread premium increased the initial teaser interest rate an entire percentage point.

Perhaps most tragic in this loan is that another mortgage broker who evaluated the loan file and served as our expert in this case determined that this homeowner was probably eligible for other, more favorable, loan products such as a Fannie Mae or Freddie Mac conventional mortgage or an FHA refinance loan.

It appears that the mortgage broker selected the loan that would pay them the highest profit, without any consideration for the homeowner's wants or needs. In this case, the mortgage was sold on the secondary mortgage, there was just no good legal basis for assignee liability and so she has been stuck in this mortgage. She is probably going to have to let the home go into foreclosure because she simply cannot afford this loan. While we have a partial Judgment against the mortgage broker, they filed bankruptcy this summer staying our case against them, although they are still licensed and in good standing with OFIS. I am doubtful that we will be able to collect any substantial damages for her.

The increased rates of foreclosure have also led to a new industry—mortgage foreclosure rescue scams. Some of the rescuers are very well qualified for this work: they work at licensed mortgage broker offices and have not one but three convictions for financial felonies. These scams take several forms, but nearly all lead to the loss of the home and the theft of thousands and thousands of dollars.

Everyone shares in the blame for what has happened here, to these homeowners and thousands like them. This legislature passed legislation in 2002 that they claimed would curb predatory lending. It did nothing but preempt local efforts to enact regulation with some real teeth. Additionally, the Consumer Protection Act, which is supposed to give consumers a remedy against unfair and deceptive practices, has become useless in this area because of recent Michigan Supreme Court rulings creating an exception so big that mortgage lenders and brokers have no problem fitting through.

Certainly a good deal of blame lies with some mortgage brokers who are taking their profits at the expense of homeowners. They defraud the homeowners, but because they have receive all their compensation up front, they do not care whether or not the homeowner can actually make their payments.

Mortgage brokers are not individually licensed, but instead are licensed by office. This allows the individuals to move from office to office with no oversight and no way to track them. Moreover, while mortgage broker offices are supposed to post a bond as part of their licensing requirements, my

recent application on behalf of a consumer for a claim against the bond was rejected because I was asking for too much money. Because the mortgage broker in this case filed bankruptcy and is no longer in business, chances are this homeowner will never see any compensation and the Judgment is basically worthless.

Lenders cannot and should not be let off the hook here. If they had looked, if they had followed their own underwriting guidelines, they would have found out that the mortgage brokers were asking for excessive fees. They would have found that homeowners could not afford the payments, especially once the interest rates began adjusting. They would have discovered that mortgage brokers were fabricating eligibility. Instead, the lenders turned a blind eye and watched their profits grow. At least until it all fell apart this year.

I appreciate that this legislature is now examining these issues. I am hopeful that you will be able to move forward with appropriate legislation that addresses these issues. While it may be too late to help these homeowners, hopefully we will be able to prevent other homeowners from losing their homes.